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UNCLAS SECTION 01 OF 02 ISTANBUL 001941

SIPDIS

SENSITIVE

E.O. 12958: N/A
TAGS: EINV ECON EFIN TU
SUBJECT: INVESTMENT CONFERENCE PRAISES TURKEY'S PROGRESS
BUT HEARS WARNING ABOUT CONTINUING RISKS

REF: A. ISTANBUL 692

¶B. ANKARA 2070
¶C. ISTANBUL 1716

This message is sensitive but unclassified-- not for internet distribution. This message was coordinated with Embassy Ankara.

¶1. (SBU) Summary: A November 8-9 investment conference organized by Turkey's Foreign Investors' Association (YASED) offered GOT policymakers a chance to highlight progress registered in recent years and to underline their readiness to accept foreign investment, whatever its source. Business participants generally applauded Turkey's achievements, while stressing that much remains to be done. Press coverage, however, focused on Johns Hopkins University economist Steven Hanke's warning of the risk of another financial crisis, as a result of the country's current account deficit and overvalued currency, which he argued parallel the conditions that preceded the country's 1994 and 2001 financial crises. Hanke, a well-known critic of IMF programs, neglected to note key differences with 1994 and 2001: a floating exchange rate and stronger fundamentals. End Summary.

¶2. (U) Open Arms: The two-day YASED Conference, optimistically titled "The New Favorite Destination for Foreign Direct Investment: Turkey, Where Opportunities Abound," brought together a range of GOT policymakers and foreign and domestic business leaders. Both Prime Minister Erdogan and State Minister Babacan used the platform to stress the Turkish government's determination to attract foreign direct investment without regard to its "color or identity." In his address to participants, Erdogan said he would welcome foreign investment "with respect, be it Arab, Jewish, or Western." He criticized those who oppose foreign investment, and in a pointed rejoinder to critics of his earlier meetings with Israeli investor Sami Ofer, who won a controversial tender for Istanbul's Galataport earlier this year (ref C), met with Ofer's son, who was attending the conference. Both Erdogan and Babacan stressed that foreign investment is critical to Turkey's future, as only it will permit the country to overcome its central economic challenge-- continued high unemployment.

¶3. (U) Still work to do: For their part, both Turkish and international business leaders repeated messages that were delivered earlier this year at Turkey's second Investment Advisory Council (IAC) meeting (ref a). They praised the country's newfound macroeconomic stability, but stressed the need for continued work to improve the country's legal and financial infrastructure. Mohammed Hariri, Vice President of the Saudi Oger Group, which won the tender for Turk Telekom, praised the GOT for the "transparency" and fairness of that privatization process, but stressed that high tax rates on telecommunications services are a real drag on the sector. A number of Gulf business leaders argued that Turkey should more actively target Gulf capital, given that it has become "more difficult" for such capital to invest in the U.S. and Europe since September 11. YASED President Saban Erdikler also pressed for action to create a national investment promotion agency under the Prime Ministry, an issue that has been stalled for years as a result of disagreements both over whether the body should be primarily private or public in nature, and over whether it should report to the Prime Minister or to Babacan.

¶4. (SBU) Clouds: Given these fairly standard messages, press attention fixed on the warning delivered by Johns Hopkins University economics professor Steven Hanke that Turkey's current account deficit and overvalued exchange rate are reminiscent of conditions that prevailed before the country's 1994 and 2001 financial crises. Hanke stressed that he is not predicting such a crisis, but simply wished to highlight risks that exist in the economy. Other participants were quick to take issue with his analysis, however-- World Bank Turkey Representative Andrew Vorkink pointed out that other elements are quite different from earlier years, in that inflation has dropped drastically and longer term foreign investments are on the rise. He predicted that FDI will increase 2-3 times in coming years. (Babacan noted that in the first eight months of the year the country received 2.9 billion USD in foreign investment; above the 1.9 billion

registered last year.)

¶5. (SBU) Comment: The YASED event broke little new ground but offered a useful opportunity for the Turkish government to take on nationalist critics who have spoken up in opposition to foreign investment in recent months. Prime Minister Erdogan in particular addressed the issue head on, both through his public comments and his meeting with Eylal Ofer. More generally, business leaders took the opportunity to highlight the fact that work is not yet done to make Turkey an attractive destination for foreign investment, and that attention needs to be paid to structural issues such as Turkey's tax and legal system. Hanke's point regarding the current account deficit is one that economists here have been grappling with for months. The need to finance a large current account deficit does make Turkey vulnerable to external shocks, as a Lehman Brothers report concluded last week. However, Hanke-- a well-known critic of IMF programs-- is in a distinct minority. Most analysts downplay the risk of a full-blown crisis. Embassy Ankara concluded in ref B that Turkey, with its floating exchange rate regime (since 2001), is more likely to experience a "correction" than a crisis if short-term investors, who currently finance the bulk of the deficit, head for the exits. The debate did put something of a damper on the conference's celebration of Turkey's progress-- "Storm warning over Turkey's economy" (from the Financial Times) was likely not the international reaction YASED was seeking. End Comment.
JONES